THE PRINCE EDWARD ISLAND ECONOMY
PROGRESS REPORT 2004

November 2004

Economics, Statistics and Federal Fiscal Relations Division
Provincial Treasury

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INTRODUCTION

This economic report summarizes the progress of the Prince Edward Island economy in 2004 to date using available statistical information which largely covers the period January to October. The report also references the national and international economic perspective. Emerging trends in economic indicators such as labour, population, prices, consumer spending, manufacturing, construction and the primary industries are identified and discussed.

The data indicate that the national economy improved significantly in 2004 while the Prince Edward Island economy experienced moderate progress. For Prince Edward Island, manufacturing and construction activity are doing well in 2004, however difficulties persist in agriculture, and retail sales and tourism are exhibiting signs of weakness. Employment gains in 2004 are up by only 0.6 per cent compared to annual growth of 2.5 per cent in 2003. The rate of unemployment averaged 11.7 per cent between January to October of this year, up from the annual rate of 11.1 per cent in 2003. From January to October 2004, consumer price inflation on P.E.I. averaged 1.9 per cent which compares to an annual rate of inflation of 3.6 per cent last year. Inflation in 2003 was driven by high prices for automotive vehicle insurance premiums and energy.

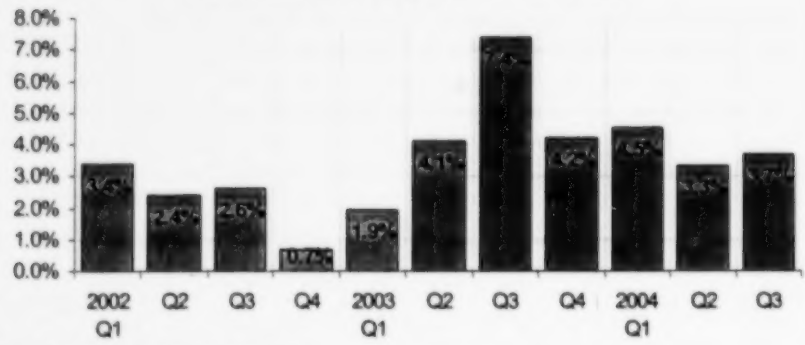
NATIONAL AND INTERNATIONAL ECONOMIC PICTURE

The U.S. economy performed well in 2003, expanding by 3.0 per cent. This compares to growth of 1.9 per cent in 2002, and 0.8 per cent in 2001. Diagram 1 shows the quarterly growth rates for the U.S. economy from 2002 to the third quarter advance estimate for 2004, as compiled by the U.S. Bureau of Economic Analysis. The economy showed significant improvement since the first quarter of 2003. Contributing to growth over this period were strong domestic spending and export activity.

Accommodative monetary policy measures by the U.S. Federal Reserve resulted in improved economic conditions. Since January 2001, when the U.S. Federal Reserve rate stood at 6.0 per cent, the Federal Reserve lowered rates 13 times in an effort to stimulate the economy which was beset

DIAGRAM 1

QUARTERLY REAL GDP GROWTH AT ANNUALIZED RATES: 2002-2004, UNITED STATES



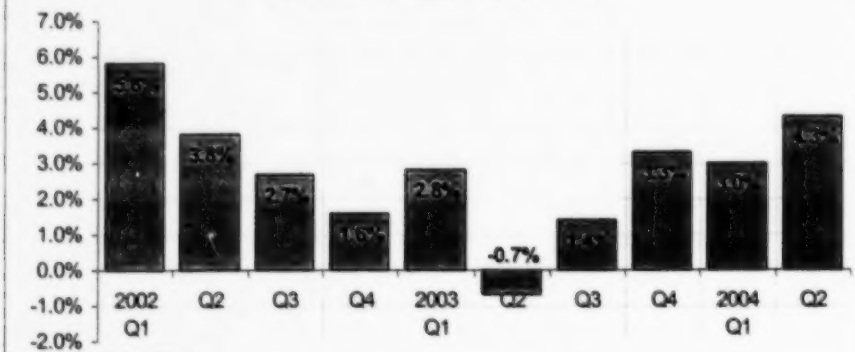
Source: U.S. Bureau of Economic Analysis

by a number of adverse developments: the collapse of the technology sector, terrorist attacks, and corporate finance scandals. The last rate cut was in June 2003 when the federal funds rate stood at 1.0 per cent, where it remained until June 2004. In view of a stronger economic position, and uncertainty relating to inflationary pressures, the Federal Reserve began to increase rates. The federal funds rate was increased in June 2004, to 1.25 per cent, and in August, to 1.5 per cent, where it currently stands.

Seasonally adjusted employment in the U.S. has improved slightly over the past three years. From January to October 2004, average employment was only 0.9 per cent higher relative to the same period in 2003. This compares to annual declines in employment of 0.3 per cent in 2003 and 1.1 per cent in 2002. The U.S. rate of unemployment averaged 5.6 per cent from January to October 2004, down from the annual rate of 6.0 per cent in 2003 and 5.8 per cent in 2002.

DIAGRAM 2

QUARTERLY REAL GDP GROWTH AT ANNUALIZED RATES: 2002-2004, CANADA



Source: Statistics Canada

The Canadian economy has shown significant improvement since the third quarter of 2003, supported by strong domestic demand and increased export activity, largely in energy exports. Diagram 2 shows the quarterly growth rates for the Canadian economy from 2002 to the second quarter of 2004.

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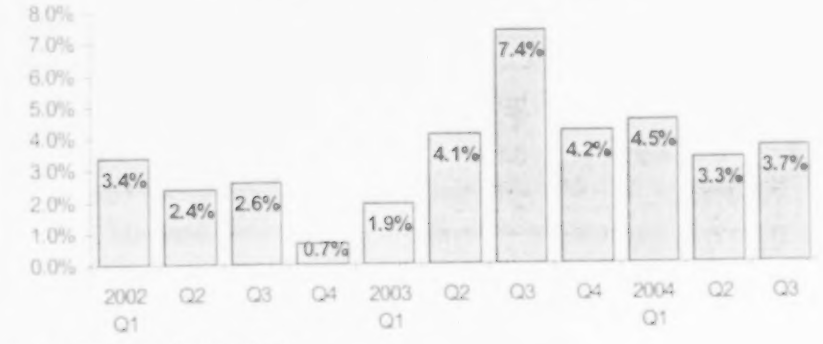

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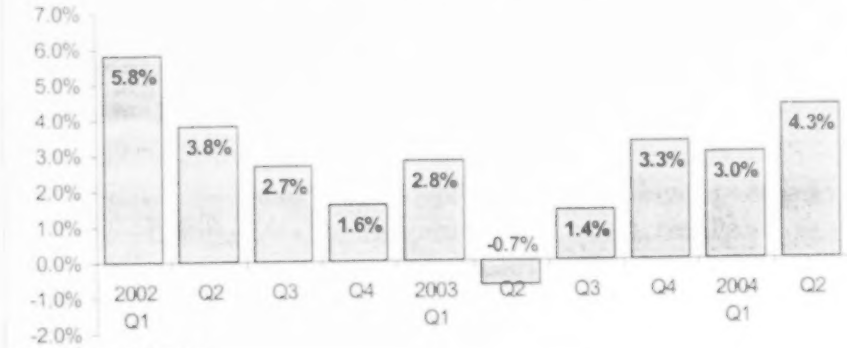

Source: Statistics Canada

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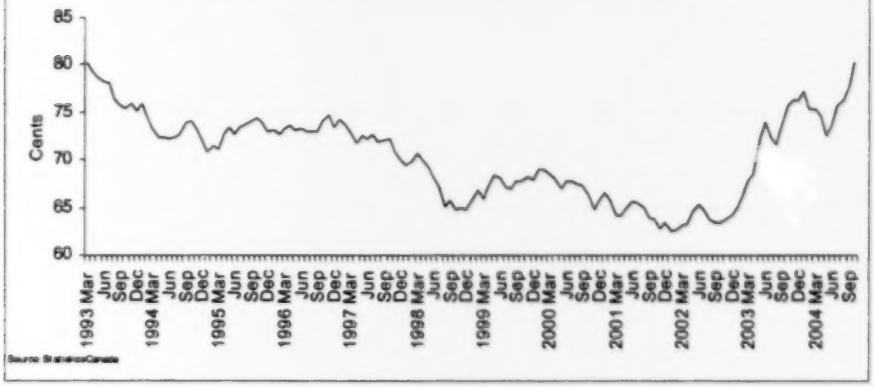
In October 2004, The Bank of Canada released its *Monetary Policy Report* which indicates that the national economy is projected to expand in the order of 3.0 per cent in 2004. This compares to growth of 2.0 per cent in 2003, and 3.4 per cent in 2002. The reduced rate of growth in 2003 was the result of a number of unforseen developments that beset both the national and provincial economies that year. These include SARS, BSE, and the rapid appreciation of the Canadian dollar relative to the U.S. dollar.

The Bank of Canada implemented accommodative monetary policy measures throughout 2003 in response to economic weakness. From April 2003 to April 2004, the Bank of Canada lowered rates five times, from a high of 3.25 per cent in April 2003 to a low of 2.0 per cent in April 2004 where it stood until September. The Bank of Canada increased rates to 2.25 per cent in September, and to 2.5 per cent in October, where it currently stands, in view of the stronger economic performance.

The Canadian dollar continued to appreciate against the U.S. dollar in 2004 following gains in 2003. Diagram 3 shows the value of the Canadian dollar relative to the U.S. currency from March 1993 to October 2004. The Canadian exchange rate with the U.S. dollar, measured by the noon spot rate, averaged 80.19 cents for the month of October 2004. This compares to 77.2 cents in January of this year, an increase of 3.9 per cent. The Canadian exchange rate in October 2004 was the highest it had been since March 1993, when it stood at 80.20 cents. Since January 2002, when the Canadian dollar relative to the U.S. dollar was 62.49 cents, the lowest level since 1950-51, the Canadian dollar appreciated by 28.3 per cent against the U.S. currency. A high Canadian dollar makes importing products less expensive and exporting products more expensive in world markets.

DIAGRAM 3

FOREIGN EXCHANGE RATES: U.S. DOLLAR PER CANADIAN DOLLAR, MAR 1993-OCT 2004



The employment situation in Canada remains positive. From January to October 2004, the average level of seasonally adjusted employment was 1.8 per cent higher relative to average employment levels during the same period in 2003. This compares to annual employment growth of 2.2 per cent in 2003 and the same in 2002. The rate of unemployment between January to October 2004 averaged

7.3 per cent, down from 7.7 per cent during the same period in 2003. The annual unemployment rate was 7.6 per cent in 2003 and 7.7 per cent in 2002.

PRINCE EDWARD ISLAND ECONOMY

The provincial economy expanded by 1.9 per cent in 2003 according to Statistics Canada, slightly lower than the national performance. For 2004, a reduced rate of growth is estimated. Provincial Treasury forecasts that the Prince Edward Island economy will expand in the order of 1.6 per cent in 2004 which compares to the 1.2 per cent forecast announced in the 2004 Budget.

The revised growth prospect for the province reflects better-than-expected performances in manufacturing and residential construction activity. Diagram 4 shows annual real G.D.P. growth for Prince Edward Island from 1998 to the revised forecast for 2004. The economy in 2003 benefitted from positive employment growth and strong residential construction activity.

DIAGRAM 4

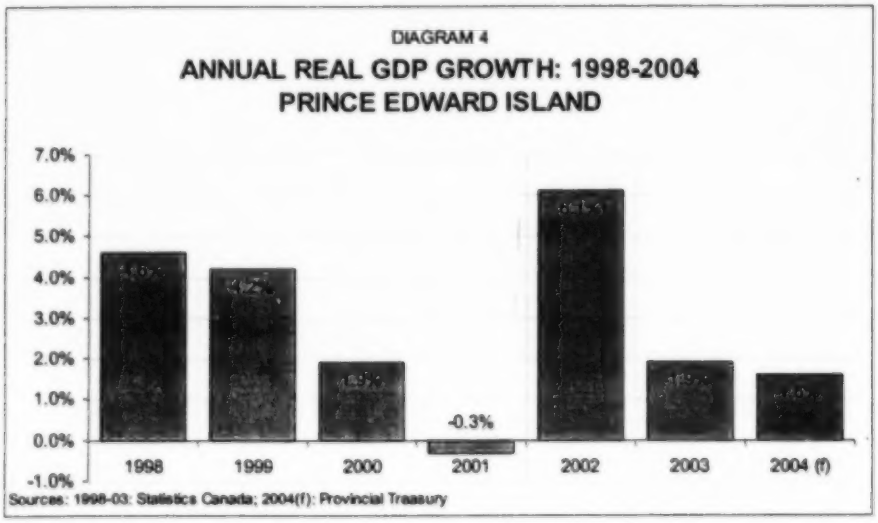


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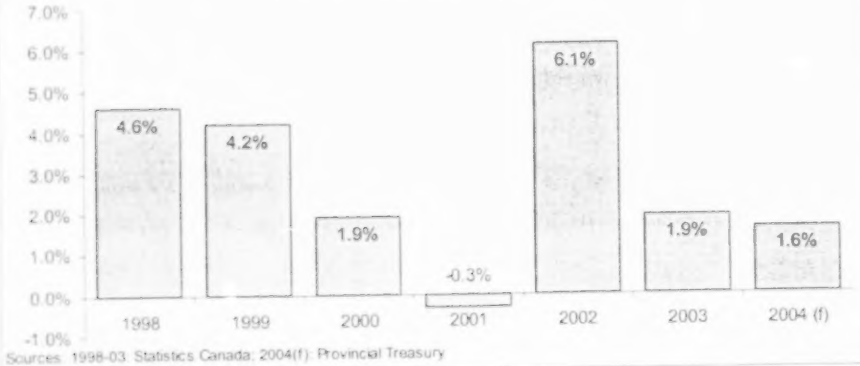
DIAGRAM 4

ANNUAL REAL GDP GROWTH: 1998-2004
PRINCE EDWARD ISLAND



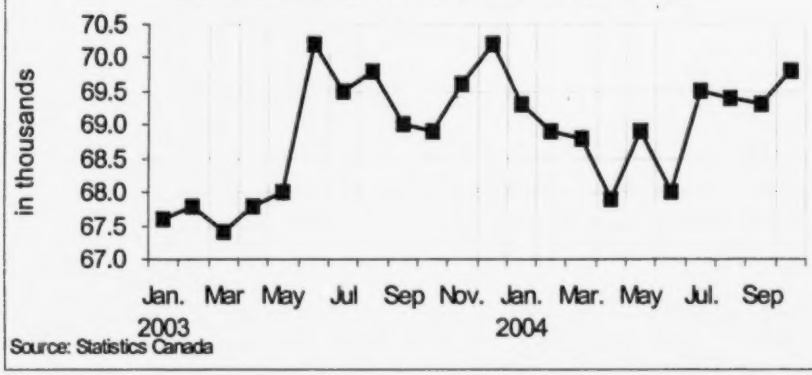
Sources: 1998-03: Statistics Canada; 2004(f): Provincial Treasury

THE LABOUR MARKET

The employment situation on Prince Edward Island has been relatively weak in 2004. Diagram 5 displays monthly seasonally adjusted levels of employment from January 2003 to October 2004.

DIAGRAM 5

MONTHLY SEASONALLY ADJUSTED EMPLOYMENT LEVELS: 2003-2004, PRINCE EDWARD ISLAND



Source: Statistics Canada

Average employment for the first ten months of 2004 is only 0.6 per cent higher relative to the same period in 2003. That year, employment rose by 2.5 per cent. As shown in the diagram, Prince Edward Island experienced strong employment gains in the second half of 2003, concentrated primarily in the services-producing sector. From January to October 2004, total employment was up by an average of 400 persons relative to the same period last year. The entire gain was in the goods-producing sector.

The seasonally adjusted unemployment rate averaged 11.7 per cent between January to October 2004, up from 11.1 per cent over the same period in 2003. The annual rate of unemployment last year was 11.1 per cent, and in 2002, 12.1 per cent.

POPULATION

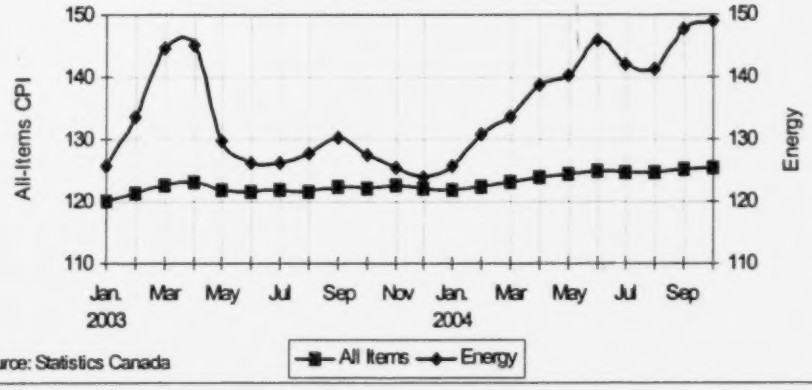
Statistics Canada estimates that the Prince Edward Island population totalled 137,864 people on July 1, 2004 compared to 137,266 a year earlier. During the twelve month period ending on June 30, 2004, the provincial population expanded by 598 people, or 0.4 per cent. Net inter-provincial migration accounted for 50 per cent of the increase, as it did in 2003, while net international migration in 2004 made up 39 per cent, compared to 18 per cent last year. Natural increase (births minus deaths) accounted for 7.0 per cent of the increase in population in 2004, down from 25 per cent in 2003.

PRICES AND RETAIL SALES

The *All Items Consumer Price Index* (CPI) for Prince Edward Island from January to October 2004, is 1.9 per cent higher relative to the same period in 2003. This compares to annual inflation of 3.6 per cent last year. Nationally, consumer price inflation averaged 1.7 per cent over the first ten months of 2004 and compares to annual inflation of 2.8 per cent in 2003. Diagram 6 compares the All-Items CPI with the Energy Price Index from January 2003 to October 2004. As the diagram illustrates, energy prices have exhibited a great deal of volatility over this period. Average energy prices from January to April 2004 were 3.7 per cent lower relative to the same period in 2003 when concerns surrounding the Iraq war caused oil prices to surge. The lower energy prices over the said period in 2004 were offset by higher prices for alcohol and tobacco. Consumer price inflation was 0.9 per cent from January to April 2004. From May to October 2004, average energy prices were 12.9 per cent higher compared to the same period in 2003. This coupled with further increases in alcohol and tobacco prices led to 2.5 per cent inflation over the May to October 2004 period. On a year-to-date basis, energy prices are 6.0 per cent higher relative to the first ten months of 2003. Crude oil prices have risen significantly since January of this year, rising from US$34.31 per barrel (based on West Texas Intermediate crude oil prices) to US$53.28 per barrel in October, an increase of 55.2 per cent.

DIAGRAM6

ALL-ITEMS CONSUMER PRICE INDEX AND ENERGY PRICE INDEX: 2003-2004, P.E.I.



Source: Statistics Canada

Seasonally adjusted retail sales on Prince Edward Island have been below the 2003 level in the first nine months of 2004, largely the result of weak automobile sales. From January to September 2004, retail sales valued $1,031.5 million, down by 0.7 per cent relative to the same period in 2003. This compares to annual growth of 0.9 per cent that year. Nationally, the value of retail sales between January to September 2004 is 4.0 per cent higher relative to the same period in 2003.

New motor vehicle sales on Prince Edward Island valued $96.4 million between January to September 2004, down 3.4 per cent relative to the same period in 2003. This compares to an annual decline of 2.8 per cent that year. Nationally, the value of new motor vehicle sales on a year-to-date

basis is 3.4 per cent lower relative to the same period in 2003. For Prince Edward Island, weakness in retail sales this year contrasts to the strong growth in labour income.

PERSONAL INCOME

For Prince Edward Island, total labour income is the largest component of personal income, comprising 58.0 per cent of the total. From January to June 2004, labour income valued $1,031.3 million, up by $51.9 million, or 5.3 per cent relative to the same period in 2003. Annual growth of total labour income was 3.9 per cent that year. Given that average employment growth on Prince Edward Island for the first six months of 2004 was only 0.7 per cent higher relative to the same period in 2003, the strong growth in labour income this year has been largely influenced by wage settlements. Nationally, total labour income during the first six months of 2004 is 3.6 per cent higher relative to the same period in 2003.

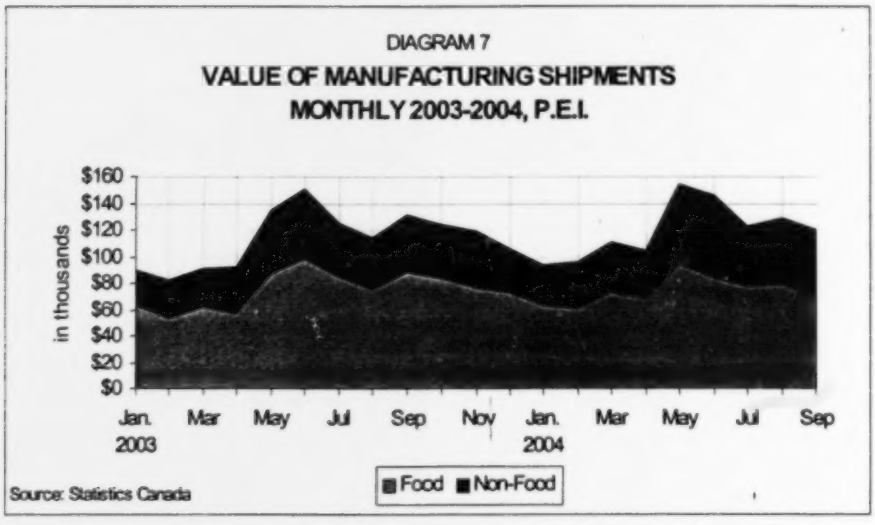
For Prince Edward Island, increased wages and salaries in health care and social services, manufacturing, and professional and personal services industries have been the major contributors to labour income growth so far in 2004. For the first six months of 2004, wages and salaries in health are 14.3 per cent higher relative to the same period in 2003. Similarly, wages and salaries in manufacturing and business services expanded by 11.0 per cent and 7.2 per cent respectively.

MANUFACTURING

Total manufacturing shipments valued $1,073.3 million over the January to September 2004 period. On a year-to-date basis, they were $65.1 million higher, up by 6.5 per cent, compared to the same period in 2003. That year, the value of manufacturing shipments rose by only 2.2 per cent in view of a drop in fish processing activity. In terms of value, the major contributors to manufacturing growth this year are transportation equipment manufacturing, and food (excluding fish) manufacturing, which is primarily made up of processed potato products.

Transportation equipment manufacturing shipments valued $145.2 million between January and September 2004, an increase of $36.2 million relative to the same period in 2003. Included in this category are aerospace products and parts manufacturing and shipbuilding and repair manufacturing. With respect to the former, Statistics Canada data indicate that aerospace products and parts manufacturing valued $120.9 million over the January to September 2004 period, an increase of $24.7 million relative to the same period in 2003. Data on shipbuilding manufacturing are not available due to confidentiality constraints.

Total food manufacturing shipments, which make up 62.2 per cent of all shipments, valued $668.2 million between January to September 2004. This is a decrease of $1.1 million, or 0.2 per cent,



relative to the same period in 2003. For the first nine months of 2004, shipments of food (excluding fish) totaled $472.7 million, up $36.4 million, or 8.3 per cent, relative to same period last year. Offsetting were shipments of fish products, valued at $195.5 million year-to-date, down $37.6 million, or 16.1 per cent, compared to the same period in 2003. Diagram 7 shows the relative importance of both food and non-food manufacturing shipments, by value, from January 2003 to September 2004.

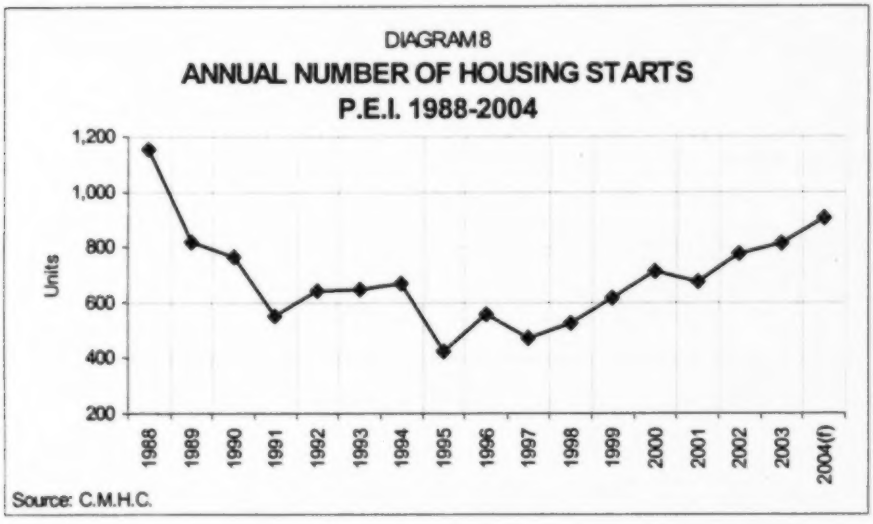
INTERNATIONAL TRADE

According to Industry Canada, Prince Edward Island's international exports of goods valued $495.0 million from January to September 2004, up 2.6 per cent relative to the same period in 2003. That year, exports fell in value by 6.2 per cent. Year-to-date growth in exports for the first nine months of 2004 can be attributed to increased exports of sawmills and wood preservation and pharmaceutical and medicine manufacturing products. Exports of tablestock/seed potatoes were down this year, by 24.5 per cent.

CONSTRUCTION AND HOUSING

Based on Statistics Canada's *2004 Private and Public Investment Intentions*, total capital expenditures for 2004 are expected to be $665.7 million. This is comprised of investment in construction, valued at $418.5 million, and in machinery and equipment, of $247.2 million. Total capital expenditures this year are up slightly from $656.5 million for 2003.

Non-residential capital expenditures are valued at $450.9 million for 2004, an increase of 0.6 per cent relative to 2003. This value is comprised of capital construction expenditures, at $203.7 million, up by 11.6 per cent from 2003, and machinery and equipment expenditures, at $247.2 million, down by 6.9 per cent. Non-residential construction this year is being driven by a number of major institutional and commercial construction projects, which include the new student residence at the University of Prince Edward Island and the Home Depot and Sears stores.



Based on estimates from Canada Mortgage and Housing Corporation (CMHC), there were a total of 720 housing starts from January to September 2004. This is a year-to-date increase of 16.3 per cent relative to the same period in 2003. According to CMHC, annual housing starts in 2004 are estimated to reach 900, the highest level since 1988 when 1,151 housing starts were recorded. Last year, there were a total of 814 housing starts. Diagram 8 shows the annual level of housing starts from 1988 to CMHC's forecast for 2004. As the diagram shows, residential construction activity has been on the rise since 1997.

TOURISM

Current indications suggest that fewer tourists visited Prince Edward Island in 2004 relative to 2003. From January to September 2004, all tourism indicators, compiled by the Policy, Planning and Research Division of Tourism Prince Edward Island are down on a year-to-date basis. Total rounds played at provincial golf courses are down by 14.0 per cent relative to the same period last year; visitation to provincial parks are down by 11.0 per cent year-to-date; visitation at visitor information centres is down by 12.9 per cent; and visits to historic sites are 15.2 per cent lower than what they were during the same period in 2003.

According to Tourism P.E.I.'s *Economic Impact Tourism 2003* document, the number of tourist parties that visited Prince Edward Island totaled 393,681 in 2003, down by 4.8 per cent from 2002.

An estimated 1,105,264 visitors came to Prince Edward Island in 2003. The tourism situation last year, in both national and provincial respects, was negatively impacted by a number of unforseen shocks. SARS, BSE and the rapid appreciation of the Canadian dollar relative to the U.S. dollar are viewed as key factors.

PRIMARY INDUSTRIES

AGRICULTURE

Farm cash receipts for Prince Edward Island in the first nine months of 2004 are below their level of the year previous. Total farm cash receipts valued $253.2 million for the first three quarters of 2004, down by 7.3 per cent compared to the same period last year. Farm cash receipts in 2003 valued $354.3 million, which is a decrease of 2.7 per cent from 2002. Table 1 shows quarterly farm cash receipts since 2003.

With respect to crops, potato receipts for the first nine months of 2004 totaled $117.7 million, a decrease of 21.8 per cent relative to the same period in 2003. That year, potato receipts totaled $186.5 million, a decrease of 2.3 per cent from 2002. Statistics Canada states that nationally, increased potato production over the last two years has resulted in lower potato prices. Based on Statistics Canada's farm product price index for Prince Edward Island, average potato prices between January and August 2004 are 11.7 per cent lower then they were during the same period in 2003.

TABLE 1
FARM CASH RECEIPTS
PRINCE EDWARD ISLAND
($ Millions)

Year/	Crops			Livestock					Direct	Total
Quarter	Potatoes	Other	Total	Cattle	Hogs	Dairy	Other	Total	Payments	
2003/1	62.7	5.3	68.0	7.2	6.5	13.4	4.6	31.8	2.7	102.6
2003/2	50.9	5.1	56.0	5.2	7.0	13.9	2.8	29.0	3.8	88.9
2003/3	36.9	13.7	50.6	1.9	6.9	13.4	3.2	25.4	6.4	81.9
2003/4	35.9	8.9	44.8	3.1	6.0	14.3	3.1	26.5	9.9	82.2
2004/1	42.0	5.5	47.5	3.3	7.4	14.4	4.1	29.9	6.4	84.2
2004/2	42.7	4.7	47.4	3.8	8.9	15.1	3.4	31.3	9.2	88.3
2004/3	32.9	13.0	45.9	2.9	9.0	15.0	3.4	30.3	4.6	80.7

Source: Statistics Canada

Based on preliminary estimates by Statistics Canada, a total of 106,000 acres of potatoes were planted this year, the same as in 2003, but down from a high of 113,000 acres in 1999. The area planted to potatoes across Canada declined by 5.3 per cent in 2004, representing the first time in 16 years that Canadian potato producers reduced their area planted.

Statistics Canada estimates that potato production on Prince Edward Island totaled 28.5 million hundredweight in 2004, up by 1.9 per cent compared to 2003. Prince Edward Island continues to be the largest potato producing province in Canada, representing 24.9 per cent of national production this year.

Livestock receipts have been seriously impacted by the B.S.E. crisis. Table 1 shows a decline in cattle receipts from $5.2 million in the second quarter of 2003, when a single case of BSE was discovered in Alberta, to $1.9 million in the third quarter. This is a 63.5 per cent drop, the largest quarterly decline in cattle receipts recorded over the past three decades on Prince Edward Island. Notwithstanding improved levels since the third quarter of last year, receipts remain well below what they were during the first half of 2003 as producers continue to contend with poor prices. For the first eight months of 2004, average cattle prices are 23.2 per cent lower than they were relative to the same period last year.

By contrast to difficult potato and cattle markets, hog receipts have strengthened considerably since the fourth quarter of 2003. On a year-to-date basis, hog receipts for the first three quarters of 2004, at $25.3 million, are 23.2 per cent higher relative to the first nine months of 2003. Hog receipts totaled $26.5 million in 2003, down by 4.3 per cent relative to 2002. Based on the farm product price index, average hog prices from January to August 2004 are 14.3 per cent higher relative to the same period last year.

FISHING

According to the Prince Edward Island Department of Agriculture, Fisheries and Aquaculture, a total of 19.9 million pounds of lobsters were landed in 2004, down slightly from 20.0 million pounds landed in 2003. Spring lobster landings this year totalled 17.7 million pounds and compares to 17.6 million pounds landed last year. Lobster prices during the Spring season were similar to what they were last year. With respect to the Fall lobster fishery, 2.15 million pounds of lobster were landed, which is a decline of 235 thousand pounds, or 10 per cent, from 2003. The decline followed changes to the existing lobster management plan for Lobster Fishing Area 25 (i.e. the Fall lobster fishery) implemented by the federal Department of Fisheries and Oceans earlier this year. Changes included a later start to the season and the introduction of a maximum size limit for both male and female lobsters. Price reports compiled by the Prince Edward Island Department of Agriculture, Fisheries and Aquaculture indicate that Fall prices toward the end of the lobster season for canners and market-sized lobsters were about equal to what they were at the same time last year.

With respect to mussel production, current indications suggest that production in 2004 will be similar to what it was in 2003, at 16,783 tonnes. Mussel prices are about equal to what they were last year. The value of mussel production in 2003, at $22.2 million, made up 77.1 per cent of the total value of aquaculture production that year. The remainder is almost entirely made up of oyster production, which was $5.7 million in 2003.

Snow crab landings on Prince Edward Island totaled 5.6 million pounds in 2004, up significantly from 3.4 million pounds landed in 2003. Of the total for 2004, Prince Edward Island fishers landed 3.2 million pounds, while the remainder was landed by fishers from other provinces. In 2003, Prince Edward Island fishers landed 2.1 million pounds of snow crab. The improvement in landings this year was due to increased quota. The landed value of snow crab in 2003 totaled $10.3 million.

PROVINCIAL GOVERNMENT

On March 30, 2004, the Honourable Mitch Murphy, Provincial Treasurer, presented his first Budget Address with the theme "*Working Together For A Secure Tomorrow.*" Budget 2004 was presented with full consolidation of provincial accounts and forecasts a consolidated deficit of $33.1 million. Spending on Health and Education was maintained for 2004-05. The Department of Health and Social Services has a Budget of $428.3 million for 2004/05, making up 40.2% of gross expenditures, and the Department of Education's Budget, at $222.7 million, makes up 20.9%. New Equalization and health care funds will be provided to the province as a result of the September and October First Ministers' Meetings, amounting to an additional $42.0 million in 2004-05 in federal transfers.

SUMMARY

Growth prospects for both the national and Prince Edward Island economies are above initial projections. The Bank of Canada's growth projection for the Canadian economy in October was revised upwards to about 3.0 per cent from the Bank's original estimate of 2.75 per cent in April 2004.

For Prince Edward Island, the economy continues to contend with difficult market conditions in agriculture and weak tourism numbers. On the positive side, exports have strengthened, goods sector employment is doing well, and potato production is up this year. Manufacturing and residential construction are strong points in 2004, performing better than what was expected at Budget. As a result, the outlook for the Prince Edward Island economy remains positive.

Inquiries can be directed to Jamie Dooks at the Economics, Statistics, and Federal Fiscal Relations Division (902) 368-4032